Market Risk Management System Checklist

"Market risk" is the risk that an insurance company will incur losses because of a change in the price of assets held (including off-balance-sheet assets) resulting from changes in interest rates, prices of securities, etc., exchange rates, and other market risk factors. ("Market-related risk" refers to this risk plus accompanying credit risks and other related risks.) There are three forms of market risk:

1) Interest-rate risk: the risk of losses because of changes in interest rates, and specifically, the risk of declining profits or losses because of changes in interest rates when an insurance company has a mismatch of interest rates and/or periods for its assets and liabilities.

2) Price fluctuation risk: the risk of a decline in asset prices because of changes in the prices of securities, etc.

3) Exchange risk: the risk of losses when an insurance company has a net asset or net liability position in its foreign-currency assets and liabilities and foreign exchange prices are different from the prices initially expected.

Inspectors will inspect the market-related risk management systems of insurance companies using "Risk Management Systems Checklists (Common Items)", "Asset Investment Risk Management System Checklist", and this checklist.

This checklist and manual apply to all insurance companies, including the foreign offices of Japanese insurance companies (foreign branch , foreign subsidiaries, and offices of the overseas workers, etc., though whether to include these offices in the inspection by this checklist and manual will be determined in light of applicable laws and ordinances, including applicable foreign-country laws and ordinances) and the Japan offices of foreign insurance companies.

Inspections on solvency margin ratio, etc. will be performed by using "(Attachment) On Inspections concerning Solvency Margin Ratio, etc." of "Real Estate Investment Risk Management System Checklist" on the basis of the checklists and manuals for "Insurance Underwriting Risk", "Asset Investment Risk"," Credit Risk", "Real Estate Investment Risk" as well as this checklist and manual.

[Notes on the use of this manual in inspections]

This manual is essentially a handbook to be used by inspectors in the inspection of insurance companies. It is expected that, as part of their efforts to ensure sound and proper operations and in accordance with the principle of self-responsibility, individual insurance companies will fully exercise their creativity and innovation to voluntarily create their own detailed manuals. These insurance company manuals should make note of the content of this manual and be adapted to the size and nature of the insurance company.

The check points in this manual represent standard to be used by inspectors in evaluating the risk management systems of insurance companies. They do not constitute direct statutory obligations to be achieved by insurance companies. Care must be taken that the manual is not adopted by rote and uniformly. If there may be cases in which the checklist description has not been fulfilled literally, by insurance company , in the light of ensuring the soundness and appropriateness of its operation only the time that the measures by insurance company are equivalent in their effects to the descriptions for the check point or are sufficient given the size and nature of the insurance company, these measures would not be deemed inappropriate.

Inspectors will therefore need to fully dialogue relevant points with insurance companies during on-site inspections.

Note: Explanation of check points

① Unless explicitly stated otherwise, items expressed in the question form such as "does the insurance company" or "is the insurance company" are minimum standards that are expected of all insurance companies. Inspectors, as they go through their checklists, need to fully verify the effectiveness of these items.

② Unless explicitly stated otherwise, items worded in the form of "it would be desirable that" constitute "best practice(sound practice)" for all insurance companies. Inspectors need only confirm these items.

Note: Distinction between "board of directors" and "board of directors, etc."

① Items that are defined as roles of the "board of directors" are items for which the board of directors itself needs to determine all essential matters. This does not, however, preclude the board of directors from delegating consideration of draft documents to the management committee or similar bodies.

② The phrase "board of directors, etc." includes the board of directors, the management committee, the management meeting, and similar bodies. Items that are defined as roles of the "board of directors, etc." would ideally be determined by the board of directors itself, but may be delegated to the management committee, etc. provided that there has been a clear delegation of this authority from the board of directors, the management committee, etc. has kept minutes of its proceedings and other materials that would allow after-the-fact confirmation, and there are adequate internal checking by the measure the results are reported to the board of directors, or auditors are allowed to participate in the management committee, etc.

Note: Explanation of "business base", "business bases", "insurance sales"

① The phrase "business base" refers to organizations other than the head office that constitute business bases, such as branch offices, business headquarters, foreign branch offices, and foreign subsidiaries. The phrase "business bases" refers to organizations other than the head office that do not engage in sales activities, such as operating bases, service centers, and foreign liaison offices.

②The phrase "insurance sales" refers to insurance agency or insurance agent and does not include insurance broker.

.

Note:

① In this checklist and manual, the phrase "policyholders" refers to insurant, insured person, insurance beneficiaries, or person targeted in sales activities or other customers.

.② When verifying status of risk management on specific cases by using this Inspection Manual, it is important to base the verification on the provisions of the Insurance Business Law, related ordinances and the Guidelines.

Types of insurance company

The types of insurance companies shall be classified as follows based on differences in their business strategies regarding market trading (including derivatives).

(1) Global Dealer (GD):

① An insurance company engaged in dealing in major financial markets.

② An insurance company that internally produces complex derivatives.

(2) General insurance companies

Insurance companies other than (1).

Every item of this checklist applies to all insurance companies, unless specifically stated [GD] type.

Inspectors will confirm that individual insurance companies clearly categorize themselves. (Note, however, that when there are substantial differences in forms of trading engaged in at individual offices, each office may categorize itself and adopt market-related risk management systems appropriate for its category.)

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
I. Recognition of risk management, etc. 1. Recognition of directors and role of board of directors	(1) Articulation of strategic goals based on management policies for the insurance company as a whole	(1) Different types of insurance companies (GD, General) will require different risk management systems. Does the board of directors clearly specify the insurance company's type?	
	(2) Construction of portfolio	(2) Does the directors recognize that constructing a proper portfolio on the basis of the limits on the investment amount of assets set by law and the nature of liabilities is in itself risk controls and does it articulate basic concepts on portfolios? Does it check portfolios regularly (at least once per quarter of the year) or as necessary? Does the directors (managing directors, in particular) recognize the nature of the portfolios constructed by the company and do they evaluate them?	
	(3) Establishment of risk management structures	(3) Does the board of directors establish appropriate market-related risk management structures in conformity with finalized strategic goals and risk management policies, and commensurate to profit targets, etc.?	
	(4) Formulation of basic concepts for establishment of limits	(4) Does the board of directors articulate basic concepts to be used in setting limits? These concepts should serve as policies for the insurance company's risk management. For example, does the board of directors set a goal of minimizing risk, or of actively taking on a certain level of risk and producing profits while managing that risk?	Note: "Limits" refers to all of the company-set limits that are necessary for risk management, such as position limits (interest-rate sensitivity and limits on notional amounts), risk limits (limits on expected losses from VaR and similar concepts), limits on asset investment (limits on holding asset), and loss-cut rules, and so throughout.
	(5) Setting of appropriate limits	(5) Does the board of directors, etc. study the risk-taking operations of individual divisions based on the basic concepts used for setting limits, and does it not just confirm the achievements but set appropriate limits for the services (purpose of holding), kinds of products, and risk categories handled by the divisions after setting limits for market divisions as a whole in light of the division's position within the overall business of the insurance company, and the owned capital, profitability, risk management capacity, personnel capacity, and claims-paying ability? Does the board of directors, etc. regularly (at least once per six months) restudy the nature of divisions' risk-taking operations and review limits? Does it confirm whether resources have been allocated appropriately throughout the company in light of the total risk limits for all market divisions from the perspective of verifying whether or not risks are excessive given its current strength level as seen from the comparison of the company's strength, as demonstrated by its capital, etc., with the risk it has taken on?	
	(6) Setting clear limits on high-risk products	(6) Does the board of directors, etc. set clear limits on high-risk products, such as complicatedly structured bonds and particularly high credit risk securities?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
2. Recognition and roles of manager	(1) Formulation of risk management rules	(1) Do market risk management rules clearly articulate the roles and authorities of the market divisions (front office), office management divisions (back office), and risk management divisions (middle office, etc.), particularly with regards to market trading (including derivatives)? Does manager establish appropriate management rules for each operations (purpose of holding), kinds of products, category risks, etc. handed by individual divisions in accordance with risk management policies and with the approval of the board of directors, etc? Does it review these rules as necessary?	Note: "Manager" refers to persons in senior managerial position in each divisions (including directors), and so throughout.
	(2) Appropriate management of limits	(2) Does manager have responsibility for providing appropriate management in accordance with the basic concepts used in setting limits and the limits set?	
	(3) Personnel management designed to prevent incidents	(3) Does manager, in accordance with the policies articulated by the board of directors, etc., have programs in place to require employees (including managers) to stay away from their jobs for a minimum of one week a year for the purpose of preventing incidents? This might include continuous leave, training, internal reassignment or any combination thereof. It is desirable that this period be at least two weeks. Does manager manage the status of these programs and ensure that they are carried out faithfully? Does manager engage in appropriate personnel ration so that specific employees are not engaged in the same jobs in the same divisions for prolonged period of time? If specific employees must be engaged in the same jobs in the same divisions for prolonged periods of time, does manager have other appropriate measures to prevent incidents from occurring?	
II. Establishment of appropriate risk management system 1. Establishment of integrated risk management structures based on the nature of liabilities ① Establishment of structures	Establishment of integrated risk management structures based on the nature of liabilities	Does the market-related risk management structures include rules on an integrated management of market-related risks based on the nature of liabilities? Does the risk management division effectively utilize the analyses and contents of transactions of the relevant divisions that perform interest rate and exchange rate forecasts, monitoring of risks, hedge transactions, monitoring of the nature of liabilities, etc. as its analytical data? Does the insurance company have a structure in place for reporting important information (is the definition of important information clearly stipulated?) of relevant divisions to the risk management division, etc.?	
② Interest-rate risk monitoring	(1) Multifaceted risk management using a variety of techniques	(1) Does the insurance company perform the multifaceted management that integrates on- and off-balance sheet products and uses different analyses method (duration analysis, simulation analysis, etc.) ?	
	(2) Analysis of interest-rate risk and use of analytical results	(2) Does the insurance company measure interest-rate risk using an appropriate financial technique regularly (at least once per quarter of the year)? Is this information used by the risk management division, etc.? It is desirable that the insurance company regularly (if possible, at least once per quarter of the year) perform stress testing and use this information in the risk management division, etc.	
③ Foreign exchange risk monitoring	(1) Appropriate monitoring of foreign exchange risk	(1) Does the insurance company appropriately manage the risks to which it is exposed, for example, by using appropriate financial techniques for the foreign exchange risks associated with foreign-currency assets and liabilities	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(2) Analysis of foreign exchange risk and use of analytical results	(2) Does the insurance company regularly (at least one per quarter of the year) measure risk and use these measurements in the risk management division, etc.? It is desirable that the insurance company regularly (if possible, at least once per quarter of the year) perform stress tests and use this information in the risk management division, etc.	
④ Price fluctuation risk	(1) Appropriate monitoring of price fluctuation	(1) Does the insurance company monitor risk factors for price fluctuation risk and appropriately manage the risk?	
	(2) Analysis of price fluctuation risk and use of analytical results	(2) Does the insurance company regularly (at least once per quarter of the year) analyze risk, for example, by measuring unrealized profits and losses, and use the analytical results in the risk management division, etc.?	
⑤ Review of limits based on the nature of liabilities	(1) Appropriate setting and review of limits	(1) Is the setting of limits on an integrated management of market-related risk based on the nature of liabilities in line with the basic policy on risk management determined by the board of directors and taking account of the insurance company's business strength, such as owned capital position and claims-paying ability? Does the company review the limits regularly (at least once per six months) or whenever necessary?	
	(2) Review of portfolio	(2) Does the insurance company review portfolios in a timely and appropriate manner when it sells securities to secure liquidity or dividends or to cut losses?	
	(3) Appropriate risk control practice	(3) Is the control of market-related risks, such as interest-rate risk, foreign exchange risk, and price fluctuation risk, practiced in accordance with the risk management policy set by the board of directors?	
	(4) Use of analytical results produced by the risk management division, etc. in management strategy	(4) Does the board of directors take into account analytical results produced by the risk management division, etc. when it formulates strategic goals and risk management policies? Does the risk management division, etc. verify that business management, such as risk control, is performed in line with the risk management policies set by the board of directors and report the result of verification to the board of directors, etc.? When the business management is found not to be in line with the policies, are improvement measures taken immediately?	
2. Management (1) Market risk management ① Customer risk management structures	(1) Establishment of structures to manage and deal with trouble with customers	(1) When customer-side risk management is insufficient, the risk is arisen, for example, customers can incur substantial losses, which may result in the insurance company being gone to law , and being suffered losses. Does the insurance company have structures in place to manage and deal with trouble with customers, including a clearly designated division to respond to disputes? Does the division responsible for dealing with troubles with customers quickly investigate the causes of the troubles and take measures to prevent recurrence?	
	(2) Development of products	(2) Does the insurance company recognize that variable insurance products, etc. can potentially have an extremely large impact on the company because of troubles with policyholders and lawsuits resulting from them? [GD] Does the company provide legal and technical checks of newly handled high-risk derivative products by the professionals of risk management and does it seek the approval of the board of directors, etc. before handling these products? Does the company refrain from developing high-risk derivative products in response to inappropriate demands from customers?	Note: "Variable insurance products, etc." includes all products managed on special accounts, and so throughout.

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(3) Sales to customers	(3) [GD] It is desirable that derivative products be sold to customers with the ability and capacity to adequately control the risks of these products. Does the insurance company respond with particular caution when customers seek to purchase derivative products for speculative purposes rather than for their own position hedges?	
	(4) Explanation of products to customers and confirmation of customer intent	(4) Does the insurance company provide appropriate and sufficient explanation to policyholders when selling products, such as variable insurance? In addition, does it have measures in place to always ask the policyholder to confirm that he/she has received explanations? [GD] In selling derivative products to inexperienced customers, does the insurance company provide specific, easily-understood documents and explanation about the nature of the product and the risks involved, including concrete examples (not just best-case scenarios but also worst-case scenarios and the amount of expected maximum loss)?	
	(5) Reporting of management performance, etc. to customers	(5) With regard to variable insurance products, etc., does the insurance company report important matters, such as management performance, to policyholders? [GD] After selling derivative products, does the insurance company provide the customer with information on the market value of the customer's position regularly or necessarily, when so requested by the customer? Do information of market value clarify how the market value is expressed (whether it takes account of hedge costs, for example)? Does the insurance company have measures to provide customers with accurate market value information, for instance, by having information provided by a risk management division (or operating division) that is in dependent of the market division?	
② Performance management	Analysis of profit/loss status and checking for inappropriate handling	Does the insurance company act improprieties such as derivative trades, etc., including purchases of structured bonds without economic reasoning, for the purpose of decorating the settlement of accounts, etc.? Should profit divisions general excessive profits, does the risk management division analyze he factors involved and verify whether or not there has been inappropriate handling that is inconsistent with rules governing risk management? Does the risk management division check profits and losses in relation to contracted values, notional principal, and trading volume?	
③ Monitoring of market value and risk	(1) Measurement of accurate market value	(1) Does the insurance company accurately measure the market value of positions (including fair value calculated by models, etc.)? Does it attempt to measure, to the extent possible, the market value of loans and other products for which there is no established technology for measuring market values? It is desirable that measurements also be made on a consolidated basis.	
	(2) Monitoring and measurement of risk factors	(2) For example, for interest rates, does the insurance company measure risk in terms of changes in the shape of the yield curve and changes in spreads of each products and each markets as well as in terms of rises (or falls) of interest rates as a whole? Does the insurance company transact the complicatedly-schemed products without measuring even risk factors? If the insurance company engages in certain degree of option trading or "writes" any options no matter how small the volume, does it measure the need for changes in hedge rates and appropriate hedging levels because of changes in market prices or changes in the expected rate of change of market prices, or because of fluctuations in market prices?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(3) Measurement of risk with uniform indicators	(3) Does the insurance company quantitatively measure risk using uniform indicators for all divisions? It is desirable that uniform indicators gasp and measure all necessary risk factors. However, should there be risks that are not adequately captured and measured by uniform indicators, does the company make business decision to ensure that all necessary factors are taken into account by complementary uniform indicators with other information that measure these risks? It is desirable that the company use VaR methods based on statistical techniques for measuring risk, but if it does not, does it use simplified measurements such as BPV? [GD] Does the insurance company use risk measurement methods that are rational and objectively and detailed formula, for example, VaR methods based on statistical techniques?	
	(4) Establishment of to verify appropriateness of model and manage model	(4) Is the appropriateness of pricing models and risk measurement models verified by organizations that are independent of the front office and organizations developing financial products (for example, by the risk management division, inspections division, or outside consultants)? Should inadequacies be found in models, are appropriate corrections made? Are structures and rules in place that do not allow the content of models to be easily changed? Are models managed appropriately and in accordance with pre-established rules? It is desirable that all models be reviewed regularly (about one per year).	
	(5) Verification of the effectiveness of risk measurement functions	(5) Does the risk management division, internal audit division, or other divisions regularly measure the impact of changes in interest rates and foreign exchange rates, etc. on the insurance company's business strength, such as profit, owned capital position, and claims-paying ability? Are measurements compared against actual profit/loss trends to verify the effectiveness of risk measurement functions?	
	(6) Appropriate implementation of stress testing	(6) VaR is a technique that only measures the maximum risk under normal market conditions. Therefore, it is desirable that the insurance company also performs regular stress testing in addition to VaR measurement. If the insurance company primarily performs sensitivity analyses based on BPV, does it regularly analyze worst-case scenarios? Is there clear rationale for the assumptions used in the stress testing and is this rationale appropriate? It is desirable that the company perform stress testing as frequently as possible (for example, about once per quarter) in relation to changes in market condition, the size of the positions it holds, and the content of its portfolio, etc.	
	(7) Frequency of position monitoring, market value appraisal, and risk volume measurement	(7) It is desirable that the insurance company monitor positions, appraise market values, and measure risk volume as frequently as possible (at least once per month) and that measurements consolidate major branches and offices. [GD] Does the insurance company make general measures at least once per day for major products on special transaction accounts?	
④ Position limit management	(1) Formulation of clear rules for limit management	(1) Does the insurance company have a clearly established structure for reporting to managers and authority (policies, procedures, etc.) for cases in which limits have been exceeded or are likely to be exceeded? Do rules prohibit the continued holding of positions in excess of position limits?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(2) Delegation of authority of limits, etc.	(2) Does the insurance company clearly specify the extent of authority given to dealers, etc. by delegating authority in writing for positions, profit targets, and limits to each managing director, manager, and dealer, and seeking the signature of the dealer, etc. to confirm all changes in limits? Does the insurance company regularly (at least once per six months) review the limits set for individual divisions?	
	(3) Compliance with rules for limit management	(3) Does the insurance company rigorously apply management rules for limits? When problems are found in rules or their application, does the insurance company make appropriate improvements? Should risk management problems be encountered, is information speedily and accurately communicated to the risk management division, etc. rather than just dealing with the problem inside the division?	
	(4) Implementation of limit and position management	(4) Does the risk management division have structures in place allowing it to monitor limits and positions on major products on at least a daily basis? [GD] Does the risk management division have structures in place allowing it to monitor limits and positions on major products during the day should there be a need to do so? Does it have and appropriately use the management computer systems of position profits by dealer and portfolio?	
⑤ Market liquidity risk	(1) Appropriate measurement of market liquidity	(1) Does the risk management division accurately measure the status of market liquidity (or receive reports thereon)? When necessary, does it report to the representative director and/or board of directors, etc. on the status of market liquidity?	
	(2) Setting and review of limits	(2) Market conditions may make it impossible to execute trades in the market at the prices initially planned for. Moreover, executing trades for a large amount of products at a time may cause a market liquidity risk of the products in question. In light of this, does the risk management division, when necessary and with the approval of the board of directors, etc. (decisions to be made by the managing director in emergencies and reported to and verified by the board of directors, etc. afterwards), set limits taking market liquidity conditions into account? Are limits regularly (at least once per six months) reviewed to take account of changes of investment products and market conditions? Are they also reviewed from time to time as necessitated by changes in conditions?	
	(3) Operations taking account of market liquidity risk	(3) Are investments made with reference to market size, depth, and liquidity for individual products? Does the insurance company recognize that executing trades for a large amount of products at one time may cause a market liquidity risk of the products in question and does it make investments taking account of such an impact?	
	(4) Monitoring	(4) Does the risk management division measure daily positions for each product and monitor changes in market size and credit status?	
	(5) Reporting	(5) Does the risk management division report measured position status, etc. accurately to the managing director (or when necessary to the representative director or board of directors) as required in the rules? If sales of products are deemed to cause liquidity risk, or if limits are exceeded, and in times of crisis or potential crisis, does it report as frequently as possible to the representative director and/or board of directors and take appropriate countermeasures?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
⑥ Operational management	(1) Operation processing in accordance with rules	(1) Does the insurance company handle foreign exchange, funds, securities trades, and derivatives thereof in accordance with applicable rules and manuals? For example: ① Does operating division monitor all trading without exception (for example, final confirmation of computer system input, confirmation with ticket stamping and serial numbers, etc.)? ② Are trading details inputted without delay? ③ Do managers approve corrections to errors in dealing tickets discovered at the confirmation/adjustment stage? ④ Are "incomplete" deal tickets (because processing will be performed in the future) appropriately managed and recorded? ⑤ Are confirmations sent by someone other than the person responsible for the trade? ⑥ Are confirmation and dealing tickets appropriately checked against each other? ⑦ Are dealing tickets, dealing sheets, and confirmations kept and stored in an appropriate manner? Is documentary evidence (for example, individual trading records) from the market division and operating division checked by the internal audit division and stored for a storage period specified in the rules (minimum of one year)?	
	(2) Data cross-checking	(2) Is trading data of the market division and operating division cross-checked? When mistakes are found, are the causes quickly investigated and corrected by procedures taken in accordance with pre-established methods? For example, in securities trading, does the insurance company regularly (at least once per month) check positions as shown in the dealing system of the market division against securities balances on the accounts of the operating division that have been confirmed with securities companies and the custody division?	
⑦ Management of credit risks associated with market trading	(1) Measurement of credit risk associated with market trading	(1) Do measurements of credit risk at least use the nominal amount method or original exposure method (nominal or contracted amount multiplied for the product or trading period)? Is the insurance company considering a switch to current exposure if it is planning to establish foreign offices in the future? [GD] Does the insurance company use the current exposure method (total replacement cost and potential exposure) to measure credit risk?	
	(2) Integrated on/off-balance-sheet management of positions, market value appraisals, and credit risk volume	(2) Does the insurance company accurately measure credit risk volume of on/off balance sheet for individual counterparties at least once per month and at any time new credit is granted or credit is renewed (or at the most recent time this has taken place)? [GD] It is desirable that the insurance company monitor individual trading for individual counterparties, that it provide integrated management of on- and off-balance-sheet market prices and credit risk volume, and that it provide information on exposures and credit limits to credit risk manager in an accurate and timely manner. Does it accurately measure credit risk volume of on/off balance sheet for individual counterparties at least once per month and at any time new credit is granted or credit is renewed (or at the most recent time this has taken place)?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(3) Clear structure for credit approval and independence of credit approval functions	(3) Does the insurance company fully study the credit risk, etc. of counterparties when selecting counterparties for trades? [GD] Does the insurance company analyze the credit risk of counterparties at least once per year? Does it set credit limits ahead of time for counterparties with which it engages in frequent and on-going trading? Are the setting, review, and management of credit limits performed by a division (credit audit division, etc.) that is independent of market-related divisions? It is desirable that the credit limits set are consistent with other credit standards.	
	(4) Formulation of credit limit rules and appropriate management of credit limit	(4) Does the insurance company have clearly defined management policies (policies on credit supplements, etc.)in the time of approaching the credit limit, and rules on reporting to managers, authorization, and procedures to be followed when credit limits are exceeded? Does the insurance company manage credit limits appropriately and in accordance with the rules? [GD] When credit risk volumes reach credit limits, does the insurance company suspend trading that would result in the extension of new credits, report to the manager as set forth in the rules (or when necessary to the representative director and/or board of directors), and decide on and implement reviews of credit limits and other responses with the approval of the manager (or when necessary of the representative director and/or board of directors)? It is desirable that the insurance company also take measures to reduce risk for existing trades, for example, by pledging additional collateral. In managing credit limits, it is effective to establish appropriate alarm points at stages prior to a counterparty's credit limit with rules for initiating discussions of supplementing credit risk measures for the counterparty when the alarm points are reached.	
	(5) Use of risk mitigation measures	(5) It is desirable that credit risk be reduced with netting contracts, pledging additional collateral, and guarantees, after having confirmed the legal validity of contracts.	
	(6) Setting of investment standards that take account of credit risks	(6) Does the insurance company set standards for securities investment by taking account of credit risks? For example, does it set standards for the selection of stocks so that it would not place too much emphasis on a specific industry or issuer (including country risk) in light of the status of loans?	
⑧ Standards of solvency margin ratio	(1) Calculation of asset investment risks associated with solvency margin ratios	(1) Does the insurance company regularly (at least once per six months) measure the volume of asset investment risks (price fluctuation risk, credit risk, subsidiary risk, off-balance trade risk, etc.) associated with solvency margin ratios in order to analyze their impact on the solvency margin ratios?	
	(2) Management of asset investment risks	(2) Does the insurance company analyze the impact on solvency margin ratios on the basis of the results of the calculation of asset investment risks? In making investments, does it take into account the results of the analysis of portfolios of asset for on-risk?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
(2) Special transaction issues (verify only for insurance companies engaged in special transaction or establishing special transaction accounts)	(1) Formulation of rules	(1) Segregated accounting requires that arbitrary decisions be eliminated and transparency assured, and this in turn requires that the board of directors, etc. formulate clear rules and that these rules be consistently adhered to. At least, does the insurance company formulate rules regarding the following matters? Does it handle these rules, etc. as important rules and does it handle changes under procedures similar to those used in formulating rules? ① Clear administrative rules for segregated accounting based on the legal definition of "special transaction purposes." * Definition of special transaction purposes * Clear organizational divisions by trading purposes (divisions of personnel into units) and independent decision-making authority Restrictions on additional post of dealers in organizations involved in special transaction and other organizations * Bans on transfers between accounts * Creation of ledgers in special transaction accounts for each type of special transaction on the account * Limits on the markets of counterparties to special transaction of securities, and recognition of hedging purposes ② Authority and responsibilities of the managers of the divisions engaged in special transaction and the managers of the divisions calculating market values, etc. ③ Compliance with rules and procedures for changing rules ④ Basic concepts for the calculation of market value, etc. * Adherence to calculation methods specified in the Insurance Business Law or other laws on in ministerial ordinances * Calculation of market value by a different organization independent of the organization engaged in special transaction * Calculation method for market value, etc. (notation when the calculation of market value, etc. is to use the "Fair Price Calculation Procedures" or other documents) * Performance of internal audits of compliance to rules regarding calculation of market prices, etc. * Method by which organizations with "front-office functions" will be involved in the calculation of market prices, etc. when there is need for their involvement ⑤ Rules and management methods for internal trading * Definition and scope of internal trading * Basic policies for internal trading * Approval of internal trades by an organization independent of front-office organizations * Approval procedures for internal trades, storage of documents ⑥ Rules for consigned trading * Performance of internal audits of compliance with rules regarding internal trading	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(2) Separation of organizations and personnel	(2) It is desirable that organizations engaged in trading for special transaction accounts (at least, organizations with "front-office functions") be at the level of units (for example, an "office," "division," or "group") or larger, and that their organization and staffing be different from the organizations engaged in trading for non-special transaction accounts on which the same kinds of trades are made but for different purposes. Organizational divisions are not necessarily required, however, when there is an objective and clear segregation of designated trades and the assets involved therein from other trades and their assets and there is little risk of accounts being manipulated (for example, when a special transaction division engages in trades other than those listed as designated trades).	
	(3) Recording in ledgers	(3) Do the books for special transaction accounts enable designated trades and the assets involved therein to be clearly segregated from other trades and the assets involved therein? Are there appropriate notations in the category ledgers created at the time applications are filed with the authorities? Are these ledgers used effectively in actual operations? (Does the insurance company refrain from using other ledgers in actual operations?)	
	(4) Prohibition against organizations trading for special transaction accounts from trading on other trading accounts	(4) Does the insurance company refrain from having organizations engaged in trading for special transaction accounts engage in trading for non-special transaction accounts (and vice versa)? (However, this does not apply when there is an objective and clear segregation of designated trades and the assets involved therein from other trades and their assets and there is little risk of accounts being decorated.)	
	(5) Prohibition against arbitrary account selection	(5) Does the insurance company refrain from making arbitrary decisions about accounts? For example, does it refrain from using special transaction accounts for trading that should be on non-special transaction accounts?	
	(6) Appropriateness of internal trading	(6) Internal trading within the same insurance company has the potential to utilize differences in accounting systems to post profits or losses. Such arbitrary handling must be eliminated. From this perspective, does internal trading appropriately complies with the "Documents Noting Matters Related to the Handling of Internal Trades" created at the time approval was received for the establishment of special transaction accounts (or with other rules governing special transaction accounts)?	
	(7) Separation of divisions involved in special transaction from divisions calculating market value	(7) Calculation method of market value must ensure that value is fair. From this perspective, does the insurance company assign different divisions to calculate market value from the divisions involved in special transaction?	
	(8) Creation and storage of materials providing basis for market value, etc. calculations	(8) Internal and external audits of the insurance company must verify the fairness of market value calculations. To facilitate this, does the insurance company keep and manage for set periods of time documents that enable market price calculations to be reproduced?	
	(9) Assurance of objectivity in fair value calculations	(9) Is the insurance company aware of the following in the assurance of the objectivity of fair price calculations? ① Does the insurance company create and consistently use "the Guidelines of Fair Value Calculation" based on rules, etc? Should there be need to modify calculation methods because of change of institution or the development of new appraisal techniques, etc., does the insurance company revise its procedures in a timely manner and in accordance with the rules, etc.? Are changes in calculation methods clearly noted?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
		② To check the internal fairness and appropriateness of the “the Guidelines of Fair Value Calculation” subject to prior approval from divisions engaged in trading for special transaction accounts (organizations with “front-office functions”) and organizations independent of organizations developing financial products (for example, the risk management division or the internal audit division, etc.)? Do the organizations above regularly check the application and administration of these procedures (for example, the risk management division or the inspections division, etc.; however, divisions performing calculations are excluded)? ③ Is assurance of the objectivity of fair value calculations included as a priority item in internal audits? Are the following included as points to be noted in audits? a) Violations of the scope of trading set by ministerial ordinance (now allowed to engage in inter-account trading for trades on exchange, securities trades, and acquisition or transfer of monetary credits) b) Effectiveness of internal checking, for example, appropriate handling of internal trading at fair value and in accordance with rules c) Clear indications of internal trades on trading tickets and segregated storage thereof d) Intentional profit/loss adjustments	
	(10) Calculation of fair value	(10) Are fair value calculations made by organizations independent of organizations with front-office functions and in accordance with the following concepts? ① Exchange trades Is value calculated using rational methods based on published closing prices (trading prices on the exchange [closing price <including liquidation price>, etc.])? ② Non-exchange trades (a) Non-exchange trades for which quotes are obtainable Is value in principle calculated using inquiry prices from brokers (including screens), business counterparty, and others? (b) Other trades a) Obtainable inquiry prices for financial products of a similar nature b) Estimates based on appraisal methods (discounted present value, option price calculation model, etc.) Is it aware of the following? ①Efforts to ensure fair calculations of the price of over-the-counter derivatives a) Are calculations generally the same for the time of the trade and the end of the accounting term? b) Are calculations checked by external auditors, such as accounting auditors? c) Are calculations checked by internal audits? ② Compliance with and consistent use of the following as defined in the “the Guidelines of Fair Value Calculation”” a) Types and sources of basic data b) Time at which basic data is obtained c) Method of creating yield curves from basic data d) Method and period of basic data storage e) Correction methods when corrections are made	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(11) Information disclosure	(11) It is necessary to disclose "important accounting policies." From this perspective, does the insurance company disclose the following matters in relation to appropriate segregated accounting and the measurement and management of objective market value? ① Framework for special transaction accounts (definition of "trading for special transaction purposes," specific lists of products covered, organizational divisions, etc.) ② Market value concepts (use of fair value concepts in market value calculations, outline of "the Guideline of Fair Value Calculation", means of assuring objectivity, etc.) ③ Financial information related to special transaction accounts	
	3. Segregation of duties Erection of mutual-checking structure	When the market divisions and operating divisions use multiple computer systems, does the risk management division obtain position information from both the market divisions and operating divisions and confirm that there are not inconsistent between them (not necessary if integrated systems are used)? Does the risk management division monitor compliance with limits and other management rules? Does it play an appropriate rule in enhancing and operating risk management structure, gathering and processing information, and reporting to the board of directors, etc.? Does the risk management division have adequate personnel to monitor trading? Does the risk management division regularly perform precise checks and analyses to search for abnormalities in the calculation of interim profits and losses (including appraisal profits and losses)? It is desirable that the insurance company has an independent risk management division staffed with experts in market trading and risk management techniques, but if it does not, does it take other measure, for example, by establishing a risk management group in the budget division? [GD] Does the insurance company have an independent risk management division staffed with experts in market trading and risk management techniques? Does the insurance company take care of the following matters regarding mutual checking functions? ① Does collusion between the chief dealer and the operating division manager place the dealers in the position of being able to directly manipulate and issue instructions regarding accounting? ② Are veteran dealers personally so trusted by superiors (managing directors, etc.) that they are considered "untouchable" by other employees? Does the insurance company recognize that human risks increase when they are dependent on specific personnel and does it carefully control this?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
		③ Are organizations run so that separations between organizations do not function? For example, is there a "confirmation team" below the market division manager or does the same person function as the manager for both the market division and the operation division? ④ Is all information communicated quickly and accurately to the risk management division? Should risk management problems be encountered, is information speedily and accurately communicated to the risk management division, etc. rather than just dealing with the problem inside the division? ⑤ Does the insurance company have an independent risk management division and is expert staff assigned to it? Is the risk management division able to report directly to the relevant directors, etc. without influence from the trading divisions? ⑥ Are recordings made of dealer trading 24 hours a day? Is the content of recordings checked against trading records using regular sampling or other techniques? Are recorded tapes stored for a set period of time (are tapes stored and managed by sections independent of the market division and operating division (for example, the risk management division) or by a section of the operation division with separate work responsibilities)? It is desirable that telephones be recorded for the operation division as well for purposes of after-the-fact confirmation. When comparing the content of dealer trading recordings with the dealing tickets (trading records), do not check dealing tickets against recordings. Rather, check whether the entire content of recordings is on the dealing ticket. ⑦ Is "so-ho" dealing only used under restricted conditions for the purpose of avoiding risks from outside hours? Does the insurance company specify trading volumes, types, and dealers? (Are there written rules?) Are answering machines and the like installed so that trading is recorded?⑧ Is the insurance company made dealers fully known that dealing recordings are regularly checked against dealing tickets?	
4. Communication	(1) Risk management division's access to information	(1) Is the risk management division able to obtain trading information and other internal data and market data from the market divisions directly and in an appropriate and comprehensive manner? Is the risk management division able to directly instruct and supervise the middle offices of other divisions?	
		(2) Does the insurance company provide a dealing support computer system to be able, at least daily, to appraise market value for the positions of each dealer and each office about all major products with which they are involved? [GD] Does the insurance company provide a dealing support computer system to be able, daily or real-time, to appraise market value for the positions of each dealer and each office about all major products with which they are involved?	
	(3) Installation of computer systems suited to operating processing	(3) Does the insurance company install and manage accounting and information computer systems that are sufficiently able to perform all basic operational processing, settlement, and management of all trading in which the company is engaged?	
	(4) Establishment of back-up structure	(4) Does the insurance company have a back-up structure, including effective contingency plans?	
	(5) Assurance of system safety	(5) Does the insurance company engage in appropriate and adequate management designed to prevent unauthorized access to computer systems, for example, management of entry and exit from work areas and use of passwords?	

Item	Risk Management System Check Point	Explanation of Risk Management Check Points	Remarks
	(6) Communication of information to the risk management division	(6) Do the market divisions, etc. communicate all information quickly and accurately to the risk management division? Should risk management problems be encountered, is information speedily and accurately communicated to the risk management division, etc. rather than just dealing with the problem inside the division?	